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IN THE HIGH COURT OF JUDICATURE AT MADRAS

DATED: 26.02.2007

CORAM

THE HON'BLE MR.JUSTICE P.D.DINAKARAN
AND
THE HON'BLE MRS.JUSTICE CHITRA VENKATARAMAN

T.C.(A).No.62 of 2004

Commissioner of Income Tax-III,
Chennai. .. Appellant

Vs.

M/s.Sharon Vaneers P. Ltd.,
Chennai .. Respondent

Appeal under Section 260A of the Income Tax Act, 1961 against the order of the Income Tax Appellate Tribunal, 'A' Bench, Chennai dated 30.5.2003 in ITA No.641/Mds/2002 for the assessment year 1994-95 and against the order of the Commissioner of Income Tax Appeal in ITA.No.366/2001-02 dated 12.03.2002.

For Appellant :Mrs. Pushya Sitaraman, Sr.SC for IT
For Respondent :Mr.K.Ravi

J U D G M E N T

(Delivered by P.D.DINAKARAN,J.)

The above tax case appeal is directed against the order of the Income-tax Appellate Tribunal in ITA No.641/Mds/2002 dated 30.5.2003, raising the following substantial questions of law.

1. Whether in the facts and circumstances of the case, the Tribunal was right in allowing the set off of the unabsorbed business losses, unabsorbed depreciation, etc. while determination of business profits under section 80HHC?
2. Whether in the facts and circumstances of the case, the Tribunal was right in holding that the provisions of section 80AB cannot be applied while determining the business profits under section 80HHC?

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2. At the outset, we find that 1st question of law is not happily worded and we reframe the same as under:

> "Whether in the facts and circumstances of the case, the Tribunal was right in holding that the unabsorbed depreciation, unabsorbed business loss and unabsorbed investment allowance of the earlier years cannot be deducted before granting deduction under section 80HHC?"

3.1. The assessment year involved in this appeal is 1994-95. The assessee computed the deduction under section 80HHC of the Income-tax Act, 1961 (in short, 'the Act') before setting off of the unabsorbed depreciation, business loss and investment allowance. But,the assessing officer computed the deduction under section 80HHC of the Act after reducing the unabsorbed business loss, unabsorbed depreciation and unabsorbed investment allowance from the profit of the business.

3.2. On appeal by the assessee, the Commissioner of Income-tax (Appeals) confirmed the order of the assessing officer.

3.3. On further appeal by the assessee, the Appellate Tribunal held that the unabsorbed depreciation, unabsorbed business loss and unabsorbed investment allowance of the earlier years cannot be deducted before granting deduction under section 80HHC of the Act, and allowed the appeal. Hence, the present appeal raising the substantial questions of law referred supra.

4. According to the Revenue, the provisions of section 80AB of the Act should be applied while determining the business profits under section 80HHC of the Act. On the other hand, the assessee contends that section 80HHC is a self-contained provision and for the purpose of deduction under section 80HHC, the computation should be made under section 80HHC(3) and section 80AB of the Act would not control section 80HHC of the Act.

5. Before proceeding further, it is apt to refer the relevant provisions of sections 80AB and 80HHC of the Act.

> "80AB. Deductions to be made with reference to the income included in the gross total income.--Where any deduction is required to be made or allowed under any section (except section 80M) included in this Chapter under the heading "C--Deductions in respect of certain incomes" in respect of any income of the nature specified in that section which is included in the gross total income of the assessee, then, notwithstanding anything contained in that section, for the purpose of computing the deduction under that section, the amount of income of that

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nature as computed in accordance with the provisions of this Act (before making any deduction under this Chapter) shall alone be deemed to be the amount of income of that nature which is derived or received by the assessee and which is included in his gross total income."

"Section.80HHC. Deduction in respect of profits retained for export business.--(1) Where an assessee, being an Indian company or a person (other than a company) resident in India, is engaged in the business of export out of India of any goods or merchandise to which this section applies, there shall, in accordance with and subject to the provisions of this section, be allowed, in computing the total income of the assessee, a deduction of the profits derived by the assessee from the export of such goods or merchandise:

.....

(2)(a) This section applies to all goods or merchandise, other than those specified in clause (b), if the sale proceeds of such goods or merchandise exported out of India are received in, or brought into, India by the assessee (other than the supporting manufacturer) in convertible foreign exchange, within a period of six months from the end of the previous year or, ~within such further period as the competent authority may allow in this behalf.

Explanation.--For the purposes of this clause, the expression "competent authority" means the Reserve Bank of India or such other authority as is authorised under any law for the time being in force for regulating payments and dealings in foreign exchange.

(b) This section does not apply to the following goods or merchandise, namely:--

(i) mineral oil; and

(ii) minerals and ores (other than processed minerals and ores specified in the Twelfth Schedule).

Explanation 1.--The sale proceeds referred to in clause (a) shall be deemed to have been received in India where such sale proceeds are credited to a separate account maintained for the purpose by the assessee with any bank outside India with the approval of the Reserve Bank of India.

Explanation 2.--For the removal of doubts, it is hereby declared that where any goods or merchandise are transferred by an assessee to branch, office, warehouse or any other establishment of the assessee situate outside India and such goods or merchandise are

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sold from such branch, office, warehouse or establishment, then, such transfer shall be deemed to be export out of India of such goods and merchandise and the value of such goods or merchandise declared in the shipping bill or bill of export as referred to in sub-section (1) of section 50 of the Customs Act, 1962 (52 of 1962), shall, for the purposes of this section, be deemed to be the sale proceeds thereof.

(3) For the purposes of sub-section (1),--

(a) where the export out of India is of goods or merchandise manufactured or processed by the assessee, the profits derived from such export shall be the amount which bears to the profits of the business, the same proportion as the export turnover in respect of such goods bears to the total turnover of the business carried on by the assessee ;

(b) where the export out of India is of trading goods, the profits derived from such export shall be the export turnover in respect of such trading goods as reduced by the direct costs and indirect costs attributable to such export ;

(c) where the export out of India is of goods or merchandise manufactured or processed by the assessee and of trading goods, the profits derived from such export shall,--

(i) in respect of the goods or merchandise manufactured or processed by the assessee, be the amount which bears to the adjusted profits of the business, the same proportion as the adjusted export turnover in respect of such goods bears to the adjusted total turnover of the business carried on by the assessee ; and

(ii) in respect of trading goods, be the export turnover in respect of such trading goods as reduced by the direct and indirect costs attributable to export of such trading goods :

Provided that the profits computed under clause (a) or clause (b) or clause (c) of this sub-section shall be further increased by the amount which bears to ninety per cent of any sum referred to in clause (iiia) (not being profits on sale of a licence acquired from any other person), and clauses (iiib) and (iiic) of section 28, the same proportion as the export turnover bears to the total turnover of the business carried on by the assessee.

Provided further that in the case of an assessee having export turnover not exceeding rupees ten crores during the previous year, the profits computed under clause (a) or clause (b) or clause (c) of this sub-section or after giving effect to the first proviso, as

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the case may be, shall be further increased by the amount which bears to ninety per cent. of any sum referred to in clause (iiid) or clause (iiie), as the case may be, of section 28, the same proportion as the export turnover bears to the total turnover of the business carried on by the assessee :

Provided also that in the case of an assessee having export turnover exceeding rupees ten crores during the previous year, the profits computed under clause (a) or clause (b) or clause (c) of this sub-section or after giving effect to the first proviso, as the case may be, shall be further increased by the amount which bears to ninety per cent. of any sum referred to in clause (iiid) of section 28, the same proportion as the export turnover bears to the total turnover of the business carried on by the assessee, if the assessee has necessary and sufficient evidence to prove that, -

(a) he had an option to choose either the duty drawback or the Duty Entitlement Pass Book Scheme, being the Duty Remission Scheme; and

(b) the rate of drawback credit attributable to the customs duty was higher than the rate of credit allowable under the Duty Entitlement Pass Book Scheme, being Duty Remission Scheme :

Provided also that in the case of an assessee having export turnover exceeding rupees ten crores during the previous year, the profits computed under clause (a) or clause (b) or clause (c) of this sub-section or after giving effect to the first proviso, as the case may be, shall be further increased by the amount which bears to ninety per cent. of any sum referred to in clause (iiie) of section 28, the same proportion as the export turnover bears to the total turnover of the business carried on by the assessee, if the assessee has necessary and sufficient evidence to prove that, -

(a) he had an option to choose either the duty drawback or the Duty Free Replenishment Certificate, being Duty Remission Scheme; and

(b) the rate of drawback credit attributable to the customs duty was higher than the rate of credit allowance under the duty Free Replenishment Certificate, being Duty Remission Scheme.

Explanation. - For the purposes of this clause, "rate of credit allowable" means the rate of credit allowable under the Duty Free replenishment Certificate, being the Duty Remission Scheme calculated in the manner as may be notified by the Central Government.

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Explanation.--For the purposes of this sub-section,--

(a) "adjusted export turnover" means the export turnover as reduced by the export turnover in respect of trading goods ;

(b) "adjusted profits of the business" means the profits of the business as reduced by the profits derived from the business of export out of India of trading goods as computed in the manner provided in clause (b) of sub-section (3) ;

(c) "adjusted total turnover" means the total turnover of the business as reduced by the export turnover in respect of trading goods ;

(d) "direct costs" means costs directly attributable to the trading goods exported out of India including the purchase price of such goods ;

(e) "indirect costs" means costs, not being direct costs, allocated in the ratio of the export turnover in respect of trading goods to the total turnover ;

(f) "trading goods" means goods which are not manufactured or processed by the assessee.

(3A) For the purposes of sub-section (1A), profits derived by a supporting manufacturer from the sale of goods or merchandise shall be,--

(a) in a case where the business carried on by the supporting manufacturer consists exclusively of sale of goods or merchandise to one or more Export Houses or Trading Houses, the profits of the business;

(b) in a case where the business carried on by the supporting manufacturer does not consist exclusively of sale of goods or merchandise to one or more Export Houses or Trading Houses, the amount which bears to the profits of the business the same proportion as the turnover in respect of sale to the respective Export House or Trading House bears to the total turnover of the business carried on by the assessee.

(4) The deduction under sub-section (1) shall not be admissible unless the assessee furnishes in the prescribed form along with the return of income, the report of an accountant, as defined in the Explanation below sub-section (2) of section 288, certifying that the deduction has been correctly claimed in accordance with the provisions of this section.

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(4A) The deduction under sub-section (1A) shall not be admissible unless the supporting manufacturer furnishes in the prescribed form along with his return of income,--

(a) the report of an accountant, as defined in the Explanation below sub-section (2) of section 288, certifying that the deduction has been correctly claimed on the basis of the profits of the supporting manufacturer in respect of his sale of goods or merchandise to the Export House or Trading House; and

(b) a certificate from the Export House or Trading House containing such particulars as may be prescribed and verified in the manner prescribed that in respect of the export turnover mentioned in the certificate, the Export House or Trading House has not claimed the deduction under this section:

Provided that the certificate specified in clause (b) shall be duly certified by the auditor auditing the accounts of the Export House or Trading House under the provisions of this Act or under any other law.

(4B) For the purposes of computing the total income under sub-section (1) or sub-section (1A), any income not charged to tax under this Act shall be excluded.

Explanation.--For the purposes of this section,--

(a) "convertible foreign exchange" means foreign exchange which is for the time being treated by the Reserve Bank of India as convertible foreign exchange for the purposes of the Foreign Exchange Regulation Act, 1973 (46 of 1973), and any rules made thereunder;

(aa) "export out of India" shall not include any transaction by way of sale or otherwise, in a shop, emporium or any other establishment situate in India, not involving clearance at any customs station as defined in the Customs Act, 1962 (52 of 1962) ;

(b) "export turnover" means the sale proceeds received in, or brought into, India by the assessee in convertible foreign exchange in accordance with clause (a) of sub-section (2) of any goods or merchandise to which this section applies and which are exported out of India, but does not include freight or insurance attributable to the transport of the goods or merchandise beyond the customs station as defined in the Customs Act, 1962 (52 of 1962).

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(ba) "total turnover" shall not include freight or insurance attributable to the transport of the goods or merchandise beyond the customs station as defined in the Customs Act, 1962 (52 of 1962):

Provided that in relation to any assessment year commencing on or after the 1st day of April, 1991, the expression "total turnover" shall have effect as if it also excluded any sum referred to in clauses (iiia), (iiib) and (iiic) of section 28 ;

(baa) "profits of the business" means the profits of the business as computed under the head "Profits and gains of business or profession" as reduced by--

(1) ninety per cent. of any sum referred to in clauses (iiia), (iiib) and (iiic) of section 28 or of any receipts by way of brokerage, commission, interest, rent, charges or any other receipt of a similar nature included in such profits ; and

(2) the profits of any branch, office, warehouse or any other establishment of the assessee situate outside India ;

(c) "Export House Certificate" or "Trading House Certificate" means a valid Export House Certificate or Trading House Certificate, as the case may be, issued by the Chief Controller of Imports and Exports, Government of India;

(d) "supporting manufacturer" means a person being an Indian company or a person (other than a company) resident in India, manufacturing (including processing) goods or merchandise and selling such goods or merchandise to an Export House or a Trading House for the purposes of export.

6. It is not in dispute that section 80HHC of the Act, which provides for deduction in respect of profits retained for export business, has been incorporated in the Income-tax Act, 1961, with a view to providing incentive for earning foreign exchange. A plain reading of section 80HHC makes it clear that in arriving at profits earned from export of both self manufactured goods and trading goods, the profits and losses in both trades have to be taken into consideration. If, after such adjustments, there is a positive profit the assessee would be entitled to deduction under section 80HHC(1) of the Act and if there is a loss the assessee would not be entitled to deduction. In arriving at the figure of positive profit, both the profits and the losses will have to be considered. If the net figure is a positive profit then the assessee will be entitled to deduction and if the net figure is a loss then the assessee will not be entitled to deduction. A plain reading of sub-section (3)(c) shows that “profits from such exports” has to be profits of exports

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of self-manufactured goods plus profits of exports of trading goods. The opening words "profit derived from such exports" together with the word "and" clearly indicate that the profits have to be calculated by counting both the exports. Deduction can be permitted under section 80HHC(1) only if there is a positive profit in the exports of both self-manufactured goods as well as trading goods. If there is a loss in either of the two, then the loss has to be taken into account for the purposes of computing the profits. On the other hand, the Section 80AB of the Act, which is also in Chapter VI-A, starting with the words "where any deduction is required to be made or allowed under any section of this Chapter" would include section 80HHC also. Further, section 80AB of the Act provides that "notwithstanding anything contained in that section". Thus section 80AB of the Act has been given an overriding effect over all other sections in Chapter VI-A. But, section 80HHC does not provide that its provisions are to prevail over section 80AB of the Act or over any other provision of the Act. Section 80HHC of the Act would thus be governed by section 80AB of the Act. [vide: IPCA Laboratory Ltd. v. Deputy Commissioner of Income-tax, 266 ITR (SC) 521].

7. In this view of the matter, we are of the view that it is not correct to say that section 80HHC of the Act is a self-contained provision and section 80 AB of the Act cannot be applied to section 80 HHC of the Act. In other words, section 80AB of the Act will prevail over any other provision in Chapter VIA of the Act and Section 80HHC of the Act would thus be governed by section 80AB of the Act. We therefore hold that the unabsorbed business losses, unabsorbed depreciation, etc. should be taken into account while computing income for the purpose of deduction under section 80HHC of the Act. The Appellate Tribunal is not correct in holding that the unabsorbed depreciation, unabsorbed business loss and unabsorbed investment allowance of earlier years cannot be deducted before granting deduction under section 80 HHC of the Act and that the provisions of section 80AB of the Act cannot be applied while determining the business profits under section 80HHC.

8. Accordingly, we answer the 1st question as reframed and also the 2nd question in the negative, against the assessee and in favour of the Revenue. The appeal stands allowed. No costs.

Sd/
Asst.Registrar

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Sub Asst.Registrar

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To

1.The Assistant Registrar,
Income Tax Appellate Tribunal,
Rajaji Bhavan,
Besant Nagar, Chennai - 90.

2.The Secretary, Central Board
of Direct Taxes, New Delhi.

3.The Commissioner of Income-
Tax (Appeals-V), Madras.

4.The Deputy Commr. of Income-tax,
Company Circle IV(6), Madras.

1 cc To Mr.Pushya Sitaraman, Advocate, SR.11544.

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